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IN THE

Supreme Court of the United States

OCTOBER TERM, 1944

No. 710

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

v.

ESTATE OF EDWARD T. BEDFORD
Title Guarantee and Trust Company, Executor,
Respondent.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

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THE COURT PRESS, N. Y. C.

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No. 710

COMMISSIONER OF INTERNAL REVENUE,
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v.

ESTATE OF EDWARD T. BEDFORD
Title Guarantee and Trust Company, Executor,
Respondent.

BRIEF FOR THE RESPONDENT

Opinions Below

The opinion of the Tax Court (R. 38-42) is reported in 1 T.C. 478. The opinion of the Circuit Court of Appeals (R. 48-51) is reported in 144 F.(2d) 272.

Jurisdiction

The date on which the judgment of the Circuit Court of Appeals was entered is discussed in Point I of the brief (*infra*, pp. 8-24). The petition for a writ of certiorari was filed on November 29, 1944. (R. 52.) The jurisdiction of this Court is invoked by the petitioner under § 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Questions Presented

1. Whether the petition for a writ of certiorari was filed within three months after entry of the judgment of the Circuit Court of Appeals as required by Section 8 of the Act of February 13, 1925, c. 229, 43 Stat. 940.

2. Whether money received by the respondent from a corporation in which it owned stock, as a part of a tax free recapitalization of the corporation, had "the effect of the distribution of a taxable dividend" within the meaning of § 112(c)(2) of the Revenue Act of 1936.

Statutes Involved

The statutes involved are set forth at pages 63-68 of the Government's brief, and need not be repeated here.

Statement

The facts in this case were all stipulated (R. 8-37). They may be summarized as follows:

Edward T. Bedford died on May 21, 1931. Included in his estate were 3,000 shares of 7% cumulative preferred stock of Abercrombie and Fitch Company (par value of $100 per share). The fair market value of these 3,000 shares on the date of the decedent's death was $210,000 (R. 8).

Because of business conditions prevailing in the following years, the Abercrombie and Fitch Company incurred losses with the result that its surplus account showed an accumulated deficit on January 31, 1936 of $399,771.87. Included in the charges against surplus were the amounts capitalized by three stock dividends paid in 1920, 1928 and 1930, aggregating $844,100 (R. 8, 37).

Because of the existence of the deficit on the company's books its credit was affected, and it had been unable for

over five years to pay any dividends on either its preferred or common stock (R. 11-12). Accordingly, a Plan of Recapitalization was proposed and submitted to the stockholders for their consideration and approval (R. 8-9, 14-15). The plan was adopted by the shareholders at a meeting held on December 8, 1936, and was accordingly put into effect (R. 8-9).

In accordance with the Plan of Recapitalization, the petitioner, as executor of the estate of Edward T. Bedford, received in January, 1937, in exchange for its 3,000 shares of 7% cumulative preferred stock ($100 par value), the following: 3,500 shares of new cumulative preferred stock of a par value of $75 per share and an annual dividend of $6 per share; 1,500 shares of the common stock of the company with a par value of $1 per share; and cash in the amount of $45,240. Thus the respondent gave up securities with an aggregate par value of $300,000, and received securities with an aggregate par value of $264,000.[1] The aggregate fair market value of the property and cash received on January 15, 1937, was $349,740 (R. 9).

For the taxable year ended January 31, 1937, the Abercrombie and Fitch Company had net earnings after taxes of $309,073.70 (R. 9).

The Tax Court, focusing its attention on the question of earnings and profits, held that there were earnings and profits, and concluded without more that the cash received was taxable as a dividend. The Circuit Court of Appeals held that the transaction was in effect a partial liquidation and thus that it did not have "the effect of the distribution of a taxable dividend" within the proper construction of § 112(c)(2) of the Revenue Act of 1936. Accordingly, it reversed the judgment of the Tax Court.

---

1. Prior to the recapitalization, the capitalization of Abercrombie and Fitch Co. was $2,000,000 in preferred stock, plus common stock with a stated value of $500,000. After the recapitalization, the capital consisted of $1,575,000 in preferred stock, and $100,000 in common, or an aggregate of $1,675,000 (R. 14).

Summary of Argument

I

The petition was not filed within three months after the entry of the judgment of the court below as required by § 8(a) of the Act of February 13, 1925. The Government relies on the "Order for Mandate" which was filled out and signed by a deputy clerk of the court below on August 29, 1944 (R. 51-52). We submit, however, that the judgment of the court was duly entered prior to that date.

The judgment of the court was rendered on August 8, 1944. That is the date its decision was filed. That is the only date upon which any act was done by the court below itself.

The judgment so rendered was entered by the clerk on August 8, 1944. He not only filed the opinion on that date, but he also made an entry in the records of the court which reads as follows:

> August 8, 1944. Order Reversed, A. N. Hand, *C.J.*

It seems clear that this is an "entry," and that it is in fact the "entry" of the judgment which had been rendered by the court. The judgment is the definitive act of the court, and that is duly recorded by the entry for August 8, 1944. Indeed, that is the only entry in the docket which connotes a judgment.

This conclusion finds support in the rules of the court below. Rule 30 provides that when "any decision" of the court is filed with the clerk, he shall "forthwith . . . enter the proper order." In the light of this rule, it appears that the order which the clerk did in fact enter "forthwith" is the entry of the action taken by the court, and thus the entry of its judgment. The same conclusion is supported by Rule 27 of the court below which states in terms that a petition for rehearing is filed with respect to a "judgment" reached by the court.

No subsequent judgment was rendered by the court, and therefore no such judgment could be entered. In all of the cases relied upon by the Government, the subsequent judgment was rendered by the judges of the court themselves. In the present case, there was no action by the judges of the court after August 8, 1944. The filling in of the order for mandate was the act of the deputy clerk alone.

The correspondence between counsel and the clerk of the court below, printed in Appendix B (pp. 71-83) of the Government's brief, when examined in its entirety, supports the conclusion for which we contend. Although the clerk made certain sweeping statements in his letter to the Solicitor General, he failed to respond to specific questions with respect to these statements. Moreover, the clerk states that the entry which he made on August 8, 1944, was made "to indicate when this court decided the case, what this court did to the lower court's judgment and who wrote the opinion." We submit that the clerk's own words show that his entry on August 8, 1944, was in law the entry of the judgment of the court.

The contention that the judgment was entered prior to August 29, 1944, is supported by the decisions. In *Medhurst* v. *S. S. "South America,"* 264 U.S. 587, it was held that the controlling date was the date on which the court below acted, and not the date on which the clerk filed the order for mandate.

This Court has recently decided several cases involving related questions. In *Department of Banking* v. *Pink*, 317 U.S. 264, it refused to accept what theretofore had been a long prevailing practice with respect to the time for filing a petition for certiorari following a judgment of the New York Court of Appeals. The decision in *Cole* v. *Violette*, 319 U.S. 581, is similar in effect to that reached in the *Pink* case. In these cases, and in *Matton Steamboat Co.* v. *Murphy*, 319 U.S. 412, this Court has

shown its intention to clarify and standardize the events defining the three months period, and to confine it to a uniform period of three months from the time when the court below has acted.

II

The reorganization of the Abercrombie and Fitch Company did not have "the effect of the distribution of a taxable dividend" within the proper construction of § 112(c)(2) of the Revenue Act of 1936. The parties are in agreement that the transaction was a recapitalization, and thus a "reorganization" as defined in § 112(g) of the Revenue Act of 1936. The sole question in the case is whether the amount of cash received on the exchange is taxable as a capital gain under § 112(c)(1) or is taxable in full as an ordinary dividend, under § 112(c)(2).

No question is raised as to the existence of earnings and profits in the corporation at the time of recapitalization. The Government's argument is in substance that wherever a corporation has earnings and profits a payment of cash in connection with a reorganization necessarily, and regardless of the circumstances, "has the effect of the distribution of a taxable dividend" within the meaning of § 112(c)(2). We believe that the Government claims too much from the statute.

The Government's construction (a) gives no effect to the controlling words which Congress wrote into § 112(c)(2); and (b) leaves no room within which § 112(c)(1) has any effective operation. Both provisions of the section can be given full and harmonious operation if proper weight is given to the "effect" clause in § 112(c)(2).

A helpful analogy in the construction of § 112(c)(2) is found in the provisions of § 115(g). The court below was correct in referring to decisions under § 115(g).

The "effect" of the transaction was that of a partial liquidation. The capital of the corporation was reduced by the transaction, and the reduction of the capital was the basic reason for carrying it out. That a liquidating distribution is not an ordinary taxable dividend was held in the leading case of *Hellmich* v. *Hellman*, 276 U.S. 233. Another case bearing closely on the present point is *Foster* v. *United States*, 303 U.S. 118. See also *Helvering* v. *Credit Alliance Co.*, 316 U.S. 107, 110, where this Court stated that "a distribution in liquidation of earnings . . . does not constitute a dividend in the proper sense of the term."

The substance of the transaction falls within the definition of a partial liquidation in § 115(i) of the statute.

None of the many cases cited by the Government on the construction of § 112(c)(2) involved a situation where the capital of the corporation was reduced as a part of the transaction. The failure to recognize the fact that the cash paid here was paid in connection with the reduction of the corporation's capital runs through the Commissioner's whole brief. The "effect" of a cash payment in connection with a reorganization depends upon the nature and circumstances of the particular reorganization. Here there was no selling out with an accompanying distribution of surplus. Instead, there was a reduction of the corporation's capital. A payment made in connection with such a transaction "has the effect of" a partial liquidation rather than the distribution of an ordinary dividend, and thus is not within the language or the purpose of § 112(c)(2).

The Committee Reports and the regulations show the inapplicability of § 112(c)(2). They show that § 112(c)(2) was designed to reach a different sort of transaction than that involved here, and particularly that it was not intended to apply to transactions which have the effect of liquidating dividends rather than of ordinary taxable dividends.

The Government's position leads to incongruities. These difficulties disappear if it is recognized that a distribution in connection with a reorganization which has the "effect" of a partial liquidation is not with the scope of § 112(c)(2).

Argument

I

The Petition Was Not Filed in Time

In its brief in opposition, the taxpayer questioned whether the Government's petition had been filed "within three months after the entry of such judgment or decree," as required by § 8(a) of the Act of February 13, 1925, 43 Stat. 936, 940. In its order granting certiorari, this Court requested counsel to discuss the question "whether the application for certiorari was filed within the time provided by law." (R. 52.)

The petition was filed on November 29, 1944. (R. 52.) This was within three months after August 29, 1944, which is the date on which a deputy clerk of the court below filled out and signed an "Order for Mandate." (R. 51-52.) If the filling in of this order for mandate was the entry of the judgment of the court below within the meaning of the Act of February 13, 1925, then the petition was filed on time. If any prior action constituted the entry of the judgment, then the petition was too late.[2]

We submit that the judgment of the court below was entered prior to the filing of its "Order for Mandate," and that that order was in fact what its title indicates, namely, the order for the issuance of the mandate. The title "Order for Mandate" connotes that it is not the judgment, but that a judgment has been previously entered.

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2. No petition for rehearing was filed, or other action taken which would suspend the running of the three-months' period.

A. The Judgment of the Court was Rendered on August 8, 1944

The opinion in this case was filed on August 8, 1944. It expressly appears in the heading of the opinion that the case was "Decided August 8, 1944." (R. 48.) "Decided" would seem to mean that what was done was a decision. This Court has declared that "The court's decision of a case is its judgment thereon." *Rogers* v. *Hill*, 289 U.S. 582, 587. We recognize, of course, that the opinion as such is not the judgment of the court. As this Court said in *Rogers* v. *Hill, supra*, "Its opinion is a statement of the reasons on which the judgment rests." But the same document may embody both the opinion, or reasons, and the decision, or judgment. Certainly the document which was filed on August 8, 1944, purports to dispose of the case finally and completely. It was not a tentative opinion to which counsel were invited to file exceptions. It is headed with the word "Decided," and it concludes with the clear and definitive statement: "The order of the Tax Court is reversed." (R. 51.) Indeed, this was the *only* act which was done by the court below itself. The judgment is the act of the court. It is a judicial act. The judgment can only be rendered by a judge. Thus it would seem clear that the decision filed on August 8, 1944, was the actual rendition of the judgment of the court. See 1 Freeman, Judgments (5th ed. 1925) § 46.

B. The Judgment so Rendered was Entered On August 8, 1944

But it may be that the important item under the Act of February 13, 1925, is not the judgment, but the entry of the judgment. We must therefore look to see when the judgment of the court so rendered was "entered." On examination, we find two items either one of which would seem to constitute the "entry" of the judgment made by

the court. First, we refer to Rule 26 of the rules of the court below, the first paragraph of which reads as follows:

> Rule 26. Opinions of the Court.
>
> 1. All opinions delivered by the court shall, immediately upon the delivery thereof, be handed to the clerk to be recorded.

Under this rule, therefore, when the opinion was handed to the clerk on August 8, 1944, it was "immediately" recorded by the clerk. This would seem to be sufficient of itself to constitute the "entry" of the judgment or decision of the court. But we need not rely upon this alone. The clerk on the same date, August 8, 1944, also made an entry in the records of the court which reads as follows:[3]

> August 8, 1944. Order reversed, A.N. Hand, *C.J.*

This is clearly an "entry," and it seems equally clear that it is in fact the "entry" of the judgment which had been rendered by the court. Let us assume that the clerk took no further action after August 8, 1944, and that a petition for certiorari was filed within three months after that date. It does not seem possible that this Court would dismiss such a petition on the ground that it was prematurely filed. If this is sound, it follows that what was done on August 8th was the entry of a judgment.

The significance of this entry stands out when the entries for August 29th are examined. These read as follows:

> August 29, 1944. Filed order for mandate.
> August 29, 1944. Issued mandate.

---

3. See the certificate by the clerk of the Circuit Court of Appeals printed in the appendix to this brief (*infra*, p. 43). The original has been filed with the Clerk of this Court.

These entries show the filing of an order for mandate on August 29th, and the issuance of the mandate on the same day. But neither the order for the issuance of the mandate, nor the actual issuance of the mandate would seem to be the judgment, as this Court's own practice clearly shows. The judgment is the definitive act of the court, and that is duly recorded by the entry for August 8, 1944.[4] Indeed, that is the only entry in the docket which connotes a judgment.

It is true that the order for mandate is entered up on a printed form which contains language reading like that often used for the entry of a judgment. But that is not important if the judgment was actually entered at an earlier date. Here, the order for mandate was simply the ministerial act of a deputy clerk, for the deputy clerk obviously has no judicial power. The only action by the court itself is that embodied in the heading and in the sentence at the end of its opinion; and the result so reached was duly "entered" by the clerk on August 8, 1944.

The Government's brief almost completely ignores this entry of August 8, 1944, and its importance in this case. The Government seeks to confine the taxpayer to the argument "that the concluding sentence of the opinion constitutes the court's judgment." (Br. 11.) The taxpayer

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4. Reference may be made to a decision of the court below, which, though directly involving practice in the district courts, is important, we believe, in showing the practice in the circuit. This case is *The Washington*, 16 F.(2d) 206 (C.C.A. 2d). The question was when a decree had been entered by the clerk of the district court. There had been delay due to the actions of the clerk. The court noted (16 F.(2d) at 207) that this was not the act of the judge. It held that the decree must be regarded as "filed" and "entered" at the time the judge acted, although the clerk did not then make an entry "in the book commonly known as the 'docket,' or 'admiralty docket.'" 16 F.(2d) at 207. But in the present case the clerk did make an entry in his docket on August 8, 1944, showing precisely what "this court did to the lower court's judgment." Clerk's letter of January 23, 1945; Government's Br. 75. The decision in *The Washington* shows that that is what the court below regards as the normal way in which a judgment is entered.

makes that argument; but it also argues that what the clerk did on August 8, 1944, constituted the "entry" of that judgment. This is evaded throughout the Government's brief. The bare fact is stated at the opening of the Government's argument (Br. 9); it is never mentioned or discussed again.

That the entry which the clerk in fact made on August 8, 1944, was the entry of the judgment finds further support in the rules of the court below. Rule 30 of its rules contains the following provisions:

> Rule 30. Taxing Costs — Order — Mandate.
>
> 1. Upon the filing of any decision by this court the clerk shall forthwith, or at any later time, if the court thinks justice requires it, enter the proper order . . .
>
> 2. A mandate may issue at any time on order of this court, but unless otherwise ordered shall issue at the expiration of fifteen days from the filing of the opinion of this court in the clerk's office unless delayed by the filing of the petition for rehearing.
>
> 3. If application for certiorari from the Supreme Court be made, application to stay the mandate shall be made only to this court, except in vacation when such application may be made to any judge of this court. . . .

The first paragraph of this rule induces the conclusion that the entry the clerk made "forthwith" on August 8, 1944, was "the proper order," and therefore the entry of the judgment. It is true that this rule provides that the order may be entered "at any later time, if the court thinks justice requires it." But here the entry was not in fact made at a later time. The clerk made the entry "forthwith" on August 8, 1944, in direct compliance with the rule. The court in no way indicated that it thought that justice required any other action. Thus, in the light of Rule 30, it appears that the order which the clerk

did in fact enter "forthwith" is the "entry" of the action taken by the court, and thus the entry of its judgment. The purpose and effect of this rule is similar to the provision now included in Rule 58 of the Rules of Civil Procedure, last sentence.[5]

The contrast between "forthwith" in paragraph 1 of Rule 30, relating to the "proper order," and "fifteen days" in paragraph 2, relating to the issuance of the mandate, is clear, and supports the conclusion, we submit, that the order which was in fact entered "forthwith" on August 8, 1944, was the entry of the judgment of the court.

Paragraph 3 of the Rule, providing for a stay of the mandate where an application for certiorari is made, makes this even clearer. An application for certiorari is filed to review a duly entered judgment. If the order for mandate itself constitutes the "entry" of the judgment, there could be no stay of the mandate. The entry of the judgment itself would command the issuance of the mandate, since that is what an "order for mandate" is. If there is to be a stay of the mandate, there must be a judgment before the mandate issues. If the judgment itself is entered by the order for *issuing* the mandate, it seems difficult to see how the mandate could at the same time be *stayed*. It could perhaps be *recalled*; but that is not what the Rule provides for. Thus this paragraph of the Rule plainly contemplates that the judgment is not entered contemporaneously with the issuance of the mandate, which would be the situation if it were held that there is no judgment except as a part of the order for issuing the mandate.[6]

---

5. This reads as follows: "The notation of a judgment in the civil docket as provided by Rule 79(a) constitutes the entry of the judgment; and the judgment is not effective before such entry."

6. The Government's brief says (Br. 13, n. 5) that this argument by the taxpayer "appears to confuse the order for mandate with the mandate itself." On the contrary, the difficulty would seem to be that the Government confuses the order for mandate with the judgment.

This conclusion is also supported by Rule 27 of the court below, which reads as follows:

> Rule 27. Rehearing.
>
> 1. A petition for re-hearing may be filed within fifteen days from the filing of the opinion of this court in the clerk's office. It must be printed, and briefly and distinctly state its grounds, and be supported by certificate of counsel; and will not be granted or permitted to be argued, unless a judge who concurred in the *judgment* desires it and a majority of the court so determines.
>
> 2. If a petition for re-hearing be filed within the time herein limited, no mandate shall issue pending the disposition of said petition. (Italics ours.)

Thus, the court below has stated its understanding that there is a "judgment" upon the filing of its opinion. The petition for rehearing is to be filed with respect to a "judgment," and it is to be filed within fifteen days. That cannot be done if there is no judgment during the fifteen-day period. Moreover, the second paragraph of the Rule provides that no mandate shall issue if a petition for rehearing is filed. From this it seems to follow that the "order for mandate," that is, the order directing the issuance of a mandate, cannot be the judgment of the court. If it were, there could be no rehearing from the "judgment," as provided in paragraph 1. Furthermore, the second paragraph of the Rule would not be necessary unless there were already a judgment when the petition for rehearing is filed, within the fifteen-day period.

C. No Subsequent Judgment was Rendered by the Court, and Thus No Such Judgment Could be Entered.

We turn next to the argument of the Government that even if there was a judgment on August 8, 1944, the "order for mandate," signed by the deputy clerk on August 29,

1944, constituted the entry of a new judgment, and that the period for certiorari began again to run from the latter date. We do not doubt that the court below has continuing power over its judgments during the term, or until the time for applying for certiorari has expired. Accordingly, the court below, by proper action of its judges could undoubtedly have vacated its judgment, or could have rendered a new judgment. If such a new judgment had been rendered by the judges, then the period for certiorari would very likely have begun to run from the date of the new judgment. But we do not believe that the deputy clerk of the court below has power, or can be given power, to render new judgments which will have the effect of superseding already existing judgments. The deputy clerk has no judicial power, and we submit that a new judgment can only be entered pursuant to judicial action.

All of the cases cited by the Government are clearly distinguishable on this ground. Thus, in *Rubber Co.* v. *Goodyear*, 6 Wall. 153, it expressly appears (p. 155) that the new judgment was signed "J. R. Bullock, District Judge." In *Silsby* v. *Foote*, 20 How. 290, it is stated (p. 295) that the second decree was "signed by the judge." In *United States* v. *Midstate Co.*, 306 U.S. 161, the record shows that the final order was signed "Welch, J." See R. 31, No. 286, October Term, 1938. Finally, in *United States* v. *Hark*, 320 U.S. 531, the second order was signed "George C. Sweeney, U. S. D. J." (320 U.S. at 533); it was the deliberate judicial act of the judge himself, and it is apparent (see especially 320 U.S. at 535) that this was an important factor in this Court's decision.[7]

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7. Similarly, in *United States* v. *Rayburn*, 91 F. (2d) 162 (C.C.A. 8th), it expressly appears (p. 164) that the second order was signed "Chas. A. Dewey, United States District Judge." The two other cases relied on by the Government (*Wright* v. *Gibson*, 128 F.(2d) 865 (C.C.A. 9th), and *Monarch Brewing Co.* v. *George J. Meyer Mfg. Co.*, 130 F.(2d) 582 (C.C.A. 9th)) are

[Footnote continued on following page.]

Ex parte Morgan, 114 U.S. 174, which the Government cites, is an authority that the clerk's act of recording a judgment is a "ministerial act." The case supports our contention that the only function of the clerk is to record the actions of the court, but that he "does not thereby render the judgments." 114 U.S. at 175.

In the present case, there was no action by the judges of the court after August 8, 1944. The filling in of the order for mandate was the act of the deputy clerk alone. It was not submitted to the court, nor signed or initialed by any of the judges of the court, nor approved by the court in any way. If we grant that the judges of the court could have rendered a new judgment, the fact is clear that they took no such action. We submit that the deputy clerk did not have power, and could not be given power, to *render* a new judgment. Therefore his action on August 29, 1944, could not start the period running again if it had already started to run from the entry made on August 8, 1944. As already pointed out, no case cited by the Government holds that an action by the clerk constitutes the rendition of a new judgment.

D. The Correspondence with the Clerk of the Court Below

Before examining further decisions bearing on the question, we will turn to a consideration of the correspondence between counsel for the parties and the clerk of the court below. At the suggestion of counsel for the taxpayer

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[Footnote continued from preceding page.]

decisions of the familiar proposition that an order which does no more than grant a motion is interlocutory, and not a final judgment.

The decision in *Puget Sound Co.* v. *King County*, 264 U.S. 22, turned upon the clear provision of the applicable Washington statute (Wash. Comp. Stat. (Remington 1922) § 11), which drew a distinction between the decision of the state court and its judgment. By the Washington law, only the later act was the judgment, and thus this alone was sufficient to start the review period.

that it might be convenient for the Court to have all of this correspondence printed in one place in chronological order, the Solicitor General has kindly set forth all of the letters in Appendix B (pp. 71-83) to his brief.

We respectfully request that the Court carefully consider all of these letters, noticing what the clerk did not state, as well as what he did. In his letter to the Solicitor General of January 23, 1945 (Government's Br. 74-78), the clerk made a number of sweeping statements, a good many of which are more in the nature of argument, or assertion of conclusions, than they are certificates of matter of fact. The clerk's arguments, of course, are entitled to no more weight than those made by counsel. In an effort to separate the clerk's arguments from his statements, counsel for the taxpayer submitted to the clerk certain specific questions. Letter of January 29, 1945; Government's Br. 78-80. The clerk's failure or inability to respond to these questions is, we submit, significant, and removes all support from much of his letter of January 23rd. We have no doubt that the clerk believes that the order for mandate which his deputy filled in on August 29, 1944, was the judgment of the court. But that is not for the clerk to decide. It is the issue here. If the entry actually made on August 8, 1944, was the entry of the judgment, then the later actions of the clerk's deputy are not enough to start the three months' period running again.

Certain portions of the clerk's letters do appear to us to be of considerable significance. We refer particularly to the fifth paragraph of his letter of January 23rd (printed at the bottom of p. 75 of the Government's brief). There, the clerk, referring to his entry of August 8, 1944 (which reads "Order reversed, A. N. Hand, *C.J.*"), says "The entry is made briefly to indicate when this court *decided the case, what this court did to the lower court's judgment* and who wrote the opinion." (Italics ours.) But the entry of when the court "decided" the case and what the court "did to the lower court's judgment" amounts

to the recording or entry of the court's judgment. We submit that the clerk's own words show that his entry on August 8, 1944, was in law the entry of the judgment of the court.

Reference should also be made to the clerk's two brief letters of January 31, 1945, and February 6, 1945 (Government's Br. 80, 83). In the first, the clerk indicates that his failure to issue the order for mandate fifteen days after the opinion was filed, as required by Rule 30, paragraph 2 of the rules of the court, was because he was waiting for the payment of costs. But it has long been settled that a judgment is final, and starts the running of the period for review, although costs are to be taxed later. *Fowler* v. *Hamill*, 139 U.S. 549. This rule is clearly recognized in the Second Circuit. *Prescott & A.C.Ry. Co.* v. *Atchison, T. & S. F. R. Co.*, 84 Fed. 213 (C.C.A. 2d); *Tuttle* v. *Claflin*, 66 Fed. 7, 8. (C.C.A. 2d); *Stallo* v. *Wagner*, 245 Fed. 636, 639-40 (C.C.A. 2d).[8]

In the second of these letters, that of February 6th (Government's Br. 83), the clerk gives as a reason for his position that the judgment is not entered until after the expiration of fifteen days, that "The fifteen-day period affords counsel for the losing party an opportunity to file a petition for rehearing." This shows, we submit, a misconception on the clerk's part as to the relation between the judgment and a petition for rehearing. It is not necessary to hold up the entry of the judgment in order to allow an opportunity for a petition for rehearing. All that is necessary to protect the losing party fully is to hold up the issuance of the mandate. That is provided for in Rule 27, paragraph 2 of the rules of the court below. The first paragraph of that rule and general practice show that the petition for rehearing is filed with respect to a judgment which has previously been entered.

8. To the same effect are *Allis-Chalmers Co.* v. *United States*, 162 Fed. 679 (C.C.A. 7th); *Crowell* v. *United States*, 281 Fed. 835 (D. Mass.); *United States* v. *Nordbye*, 75 F.(2d) 744, 746 (C.C.A. 8th); *Sosa* v. *Royal Bank of Canada*, 134 F.(2d) 955, 956 (C.C.A. 1st).

We submit, therefore, that the net effect of the exchange of correspondence is to support the taxpayer's position in this case.

E. The Decisions Support the Contention that the Judgment was Entered Prior to August 29, 1944.

The question of the date of entry of judgments in the Second Circuit has previously been a source of difficulty.

In *Medhurst* v. *S. S. "South American,"* 264 U.S. 587, the body of the order for mandate carried the date October 15, 1923. On the back, it was marked "Filed, October 16, 1923." The case was docketed in this Court on January 16, 1924, and the Court denied certiorari "for failure to file within the time prescribed by the statute." Examination of the record in this case, as filed with the Clerk of this Court, shows that the order for mandate was initialed "H.W.R." and "J.M.M." The case was heard before Rogers, Hough and Mayer, *JJ.*, and these are the initials of Judges Rogers and Mayer. Thus, in this case the order for mandate was the judicial action of the court. The case, therefore, is an authority in favor of the taxpayer's position here; for it decides that the important date is the date when the judges act (October 15, 1923), and not the date when the clerk does something (October 16, 1923, in that case). It would seem quite as clear in the present case as in the *Medhurst* case that the act of the clerk was purely ministerial, and neither could nor did extend the time for review.

Of course the *Medhurst* case is not a decision that the petition there would have been filed on time if it had been filed within three months after October 15, 1923. That question was not presented. Even if it had been decided there, it would not control here because there the order for mandate was the judicial act of the Judges, while here it was issued solely by the deputy clerk.

In *Cahill* v. *Mayflower Bus Line, Inc.*, 296 U.S. 629, the order for mandate was dated and filed on June 17, 1935. The petition was filed September 21, 1935. This was within three months from the date on which the judgment pursuant to the mandate was entered in the trial court. This Court denied the petition for failure to file on time.[9] This does not affect the present case, as it is not a decision that the petition would have been on time if it had been filed by September 17, 1935. The petitioner's action in that case, however, was in accordance with common New York practice (*cf. Department of Banking* v. *Pink*, 317 U.S. 264, discussed below), and the Court's action is therefore significant as showing that the specific requirements of the statute as to the time within which a petition must be filed are not affected by practices or understandings as to the time when the period begins to run.

Finally, reference may be made to *Helvering* v. *Lerner Stores Corp.*, certiorari granted, 314 U.S. 598, decided on the merits, 314 U.S. 463. Here the opinion was filed on March 24, 1941. The order for mandate was filed April 12, 1941. The petition was filed in this Court on July 8, 1941. The question whether the petition was filed on time was raised by the taxpayer in his brief in opposition. The taxpayer argued that the opinion was the judgment. He did not show, as we have done here, that the clerk actually made an "entry" in his records on the same date, showing the action of the court. Neither did the taxpayer rely on the terms of Rules 27 and 30 of the court below. This Court granted certiorari, and decided the case on the merits. It is clear, however, that it did not "decide" any question as to the jurisdiction, because the question was abandoned by the taxpayer in his brief on the merits. In that brief (p. 1), under "Jurisdiction," the taxpayer stated that the judgment below "was entered April 12, 1941 (R. 31)." The issue was not mentioned in either the tax-

9. The same result was also reached in a similar situation in *Warshauer* v. *Lloyd Sabaudo, S.A.*, 293 U.S. 610.

payer's or the Government's briefs. There is no reference to it in the opinion of this Court.

It is true that in the *Lerner Stores* case, and doubtless in other cases, this Court has rendered decisions in cases where it did not have jurisdiction, if our position is correct. That is, of course, no reason for deciding the present case without jurisdiction. In no previous case has the question actually been decided by the Court. "Questions which merely lurk in the record" (*Webster* v. *Fall*, 266 U.S. 507, 511) are not decided by the Court. Moreover, a decision in favor of the taxpayer on the jurisdictional question here would not affect the validity of any of those decisions. Under a now familiar line of cases, the question of jurisdiction in those cases is now *res judicata*, and beyond question by the parties. *Stoll* v. *Gottlieb*, 305 U.S. 165; *Chicot County Drainage District* v. *Baxter State Bank*, 308 U.S. 371; *Jackson* v. *Irving Trust Co.*, 311 U.S. 494.

This Court has recently decided several cases involving related questions. In *Department of Banking* v. *Pink*, 317 U.S. 264, it refused to accept what theretofor had been a long prevailing practice with respect to the time for filing a petition for certiorari following a judgment of the New York Court of Appeals. It would appear that the practice which was rejected there was strictly analogous to the practice upon which reliance was rested in this case. Under that practice, something done after the action of the court which decided the case had been regarded as the judgment for the purpose of starting the review period. The decision in the *Pink* case was that there was no reason for a different period of review for decisions of the New York Court of Appeals from that applied in reviewing the decisions of other State courts. For similar reasons, there would seem to be no reason for perpetuating a special period of review for decisions of the Second Circuit Court of Appeals. As shown by

the letters summarized in Appendix C (pp. 85-88) of the Government's brief, no other circuit has a practice like that which is followed by the Second Circuit.

If the "order for mandate" were in all cases filed fifteen days after the Court's decision is made, the matter might not be serious, although there is no particular reason for automatically adding fifteen days to the period prescribed for review. But, in the present case the delay was actually twenty-one days. In *International Standard Electric Corp.* v. *Commissioner*, Nos. 739-740, October Term, 1944, the period was twenty-nine days. Reference may also be made to two recent cases which have come to our attention. In *Katz* v. *Horni Signal Mfg. Corp.*, 145 F.(2d) 961 (C.C.A. 2d), a petition for rehearing was denied December 20, 1944. The order for mandate was filed February 9, 1945, an interval of 51 days. In *United States ex rel. Reed* v. *Badt*, 141 F.(2d) 845 (C.C.A. 2d), the court's decision was rendered on April 13, 1944. The order for mandate was filed June 13, 1944, two months later. It is also relevant to point out that in this case the order for mandate was filed 17 days *before* the clerk's fees were paid, which, according to his records, was on June 30, 1944. Thus the clerk's explanation (in his letter of January 31, 1945; Government's Br. 80), even if material, which we by no means concede, does not represent the consistent practice in the Second Circuit.[10] In all of these cases, as here, the clerk made an appropriate "entry" on the date on which the court actually rendered its decision.

These illustrations show that after a decision is reached by the Second Circuit Court of Appeals, the time for the review of that decision, if the practice on which the Gov-

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10. Indeed, the reference to the payment of fees merely aggravates the situation. If the entry of the judgment is to be held up until the clerk receives his fees, the prevailing party can postpone review indefinitely by simply failing to pay the fees. This would clearly be contrary to the intention of Congress in fixing the three months' limit on the review period.

ernment relies here is upheld, is extended for a length of time which varies from case to case, not by any action by the court itself, but solely by the clerk, or his deputy, in determining when he will fill out the order for mandate. This, we submit, is an unsound practice, inconsistent with the basic intention of Congress in prescribing the three months' limitation, and contrary to the terms of the rules of the court below. The clerk's argument on this point, near the end of his letter of January 23rd (Government's Br. 78), and the similar argument by the Government (Br. 20-21) amount to no more than a begging of the question. Of course, if the order for mandate is the judgment, then there is only a period of three months from that date. But if some prior action is in fact the entry of the judgment, then the three months' period is extended if it is made to run from the date of the order for mandate. To treat the latter order as the point at which the three months' period begins to run does, *in substance*, we submit, allow a different period for review of judgments for the Second Circuit from that applied in all other circuits, and is contrary to the underlying purpose of Congress in prescribing the three months' review period.

The decision in *Cole* v. *Violette*, 319 U.S. 581, is similar in effect to that reached in the *Pink* case. Again local practice was held not to be controlling. In *Matton Steamboat Co.* v. *Murphy*, 319 U.S. 412, this Court decided a somewhat related question contrary to the conclusion reached in Robertson and Kirkham, Jurisdiction of the Supreme Court of the United States, pp. 717-18. In reaching this result, the Court referred (319 U.S. at 415) to the uncertainties and delay which would result from a different conclusion. We submit that similar uncertainties and delays result from leaving the start of the three months' period to the time when the clerk or his deputy chooses to act. In all of these recent cases, *Pink*, *Cole* and *Matton*, this Court has shown its intention to clarify

and standardize the events defining the three months' period, and to confine it to a uniform period of three months from the time when the court below has acted. The application of these principles here leads to the conclusion that the petition in this case was not filed on time.

We submit that the judgment was entered on August 8, 1944, that no act by the court constituted the rendition of a new judgment thereafter, and that consequently the petition filed on November 29, 1945, was filed too late.

II

The reorganization of the Abercrombie and Fitch Company did not have "the effect of the distribution of a taxable dividend" within the proper construction of Section 112(c)(2) of the Revenue Act of 1936.

Throughout this proceeding, the parties have agreed that the exchange which the taxpayer made with Abercrombie and Fitch Co. in January, 1937, was in connection with a recapitalization, and thus was a "reorganization" as defined in § 112(g) of the Revenue Act of 1936. Since cash was received on the exchange, § 112(c) of the statute (Government's Br. 64) comes into operation. The sole question in the case is whether the amount of that cash is taxable as a capital gain under § 112(c)(1), or is taxable in full as an ordinary dividend under § 112(c)(2).

This question turns on the proper construction of the words "has the effect of the distribution of a taxable dividend" in § 112(c)(2). We submit that the cash payment here did not have "the effect of the distribution of a taxable dividend," and that § 112(c)(2) therefore has no application. If this argument is correct, then § 112(c)(1) does apply, and the gain should be taxed as a capital gain.

A. Earnings and Profits

The Government devotes nearly ten pages of its brief (Br. 23-32) to an argument that Abercrombie and Fitch Co. had earnings and profits at the time of the recapitalization in an amount at least equal to the amount of cash which it paid out. No contention to the contrary was made in the court below. This was expressly stated in our Brief in Opposition (p. 10), as the Government recognizes at the end of its discussion of the question (Br. 32). It is difficult to see, therefore, why the question should be argued at such length in the Government's brief. This unnecessary argument should not divert the Court's attention from the question which is involved in the case.

As already indicated, that question relates solely to the proper construction of § 112(c)(2) of the Revenue Act of 1936, which applies only to payments which have "the effect of the distribution of a taxable dividend." It was to this point only that the attention of the court below was directed. In this light, the citations in the court's opinion of *Commissioner* v. *Quackenbos*, 78 F.(2d) 156 (C.C.A. 2d), and *DeNobili Cigar Co.* v. *Commissioner*, 143 F.(2d) 436 (C.C.A. 2d), were not in any way nor to any extent a decision that the corporation here did not have earnings and profits. They were cited in support of the decision, and, we submit, the proper decision, that regardless of earnings and profits the payment here did not have "the effect of the distribution of a taxable dividend."

We turn then to the question of the construction of § 112(c)(2).

B. Section 112(c)(2) of the Revenue Act of 1936 Does Not Make All Cash Payments in Connection with a Reorganization Taxable as a Dividend Merely Because there are Earnings and Profits.

The Government's position is based on its contention (Br. 42-43) that § 112(c)(2)—

> applies to *any distribution* in a reorganization *if there are earnings and profits* to cover it, without any limitation as to the time and manner in which the distribution may have been made. (Italics ours.)

This argument runs through the Government's brief. It is also stated on page 35, again on page 40, on page 46, and elsewhere. We believe that the Government claims too much from the statute.

In the first place, let us look at what Congress actually said. In § 112(c)(2), Congress provided that—

> If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection *but has the effect of the distribution of a taxable dividend*, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. . . . (Italics ours.)

The Government simply excises from the statute the whole phrase which Congress wrote restricting this provision to situations where the payment "has the effect of the distribution of a taxable dividend." The Government says that the section applies *wherever* the corporation has earnings and profits. That is not what Congress said; and if Congress had meant that it could easily have

written it that way. The fact that Congress wrote the provision the way it did shows that it was not intended to apply automatically wherever the corporation has earnings and profits. *Helvering* v. *Griffiths*, 318 U.S. 371.

Another way to put the same argument is to point out that the Government's construction gives no scope whatever for § 112(c)(1). Under the Government's view, § 112(c)(2) would apply in every case. To the extent that there were earnings and profits, the payment would be taxed as a dividend under the first sentence of § 112(c)(2). Any balance of the payment (which would be all of the payment where there were no earnings and profits) would be taxed as a capital gain under the second sentence of § 112(c)(2). *Section 112(c)(1) would never operate at all.*

Both the structure and the history of § 112(c) show that § 112(c)(1) was intended to state the general rule, while § 112(c)(2) was subsequently added to the statute to take care of the special and unusual case where § 112(c) is used as a cloak for what is in substance the distribution of a taxable dividend. But the Government's construction (a) gives no effect to the controlling words which Congress wrote into § 112(c)(2), and (b) leaves no room within which § 112(c)(1) has any effective operation. It would seem that such a construction of the statute would have to be rejected. Both provisions of the section can be given full and harmonious operation if proper weight is given to the "effect" clause in § 112(c)(2).

We turn then to a consideration of the construction of these words which the Government simply eliminates from the statute. Did the payment here have "the effect of the distribution of a taxable dividend"? We submit that it did not. This is a question of statutory construction, a question of law to be decided by the Court. *Security Flour Mills Co.* v. *Commissioner*, 321 U.S. 281; *Claridge Apartments Co.* v. *Commissioner*, 323 U.S. 141, 145. *Cf. Virginian Hotel Corp.* v. *Helvering*, 319 U.S. 523.

Congress specifically declared that one of the "questions of law" which the courts are to consider on review is "the proper interpretation and application of the statute or any regulation having the force of law." House Report No. 1, 69th Cong., 1st Sess. (1925) p. 19; Senate Report No. 52, 69th Cong., 1st Sess. (1926) pp. 36-37.

C. The Analogy to § 115(g)

One of the ways to approach this question is to look for analogies. There is, in fact, a section which contains language, and has a function, very closely analogous to that of § 112(c)(2). This is § 115(g), which applies to cases where a corporation cancels or redeems its stock at such time and in such manner as to be "essentially equivalent to the distribution of a taxable dividend." This language is not the same as that in § 112(c)(2), but it is very similar. There is certainly not much difference between "essentially equivalent to" and "has the effect of."

Thus, the court below properly considered cases arising under § 115(g). It did not confuse § 115(g) with § 112(c)(2). It recognized that § 115(g) was only an analogy; but it concluded properly that § 115(g) furnished a close analogy, and a valuable guide to the proper construction of § 112(c)(2). On this basis, it concluded that the payment made in this case would not have come under § 115(g). There are no controlling decisions of this Court on the proper construction of § 115(g). The construction of § 115(g) which the court below reached was, however, in accordance not only with its own decisions, but also with those of other circuits. *Commissioner* v. *Brown*, 69 F.(2d) 602 (C.C.A. 7th); *Hyman* v. *Helvering*, 63 App. D. C. 221, 71 F.(2d) 342; *Commissioner* v. *Cordingley*, 78 F.(2d) 118 (C.C.A. 1st). Although some of the language in the opinions of the court below may go quite far, there does not seem to be any reason to adopt

the Government's construction of § 115(g), which is, essentially, that all redemptions of preferred stock necessarily come within its scope. Regardless of the applicability of the decisions of the court below to other facts, it would seem sound in holding that the present situation would not have fallen within a proper construction of § 115(g).

D. The "Effect" of the Transaction was that of a Partial Liquidation

Turning again to the language of § 112(c)(2), we may ask: What was the "effect" of the transaction here? Of course, the transaction *was* a recapitalization, and thus a reorganization, but we are now focusing attention upon its "effect."

When § 112(c)(2) refers to a distribution which has "the effect of the distribution of a taxable dividend," we submit that it applies to a distribution which has the effect of an ordinary dividend taxable under § 115(a), and that it does not apply to a distribution of the sort which has the effect of a distribution in partial liquidation to which § 115(c) would apply were it not made as a part of a recapitalization, and thus governed by § 112(c). We submit that the "effect" of the transaction in the present case was that of a partial liquidation and not that of an ordinary or taxable dividend.

1. In the *first* place, it was similar in effect to a liquidating dividend because there was in fact a partial liquidation of the corporation. Its capital was reduced by the transaction, and the reduction of the capital was the basic reason for carrying out the transaction. Each old preferred share, representing $100 par value, was exchanged for 1 1/6th new preferred shares of a par value of $75 per share, and ½ share of $1 par value common stock. (R. 12-13.) Thus each old $100 par value received

new stock with a par value of $88.[11] This was obviously a reduction of the corporation's capital.[12] Each shareholder's stake in the enterprise was reduced. And it was not a *pro forma* reduction. It was a real and necessary reduction designed to remove a surplus deficit from the corporation's books, a necessary step before it could resume the payment of dividends in accordance with the governing state law.

That a liquidating distribution is not an ordinary taxable dividend was held in the leading case of *Hellmich* v. *Hellman*, 276 U.S. 233. It is interesting to note in that case that it was the Government which contended the transaction was taxable as a liquidating rather than as an ordinary dividend, and the Government's argument was sustained. In reaching its result, the Court said (p. 237):

> However, when § 201(a) and § 201(c) [corresponding to § 115(a) and § 115(c) of the 1936 Act] are read together, . . . we think it clear that the general definition of a dividend in § 201(a) was not intended to apply to distributions made to stockholders in the liquidation of a corporation, but that it was intended that such distribution should be governed by § 201(c). . . .

Of particular importance in this connection, is the decision in *Foster* v. *United States*, 303 U.S. 118. In that case, the corporation distributed $1,025,000 in 1929 in liquidation of 500 shares of its own stock. The question at issue was whether this distribution had reduced its earnings and profits so that a subsequent distribution

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11. The petitioner had 3000 old preferred shares of a par value of $100 each (R. 3), or a total par value of $300,000. It received 3500 new preferred shares of a par value of $75 each, and 1500 common shares with a par value of $1 each (R. 3), or a total aggregate par value of new stock of $264,000.

12. The total capitalization of the company was reduced from $2,500,000 to $1,675,000. (R. 14.)

would not be taxable as a dividend. This Court held that the distribution in 1929 was governed by § 115(c) and not by § 115(a), with the result that it was not chargeable against earnings and profits. On the same reasoning, it follows that the distribution here had the effect of a liquidating distribution and not that of a taxable dividend.

Reference may also be made to *Helvering* v. *Credit Alliance Co.*, 316 U.S. 107, where the Court held that a corporation was entitled to a dividends paid credit for a liquidating distribution because of the express provision of § 27(f) of the Revenue Act of 1936, which is applicable in terms only to the computation of the dividends paid credit under that section. Except for that express provision, the Court recognized (p. 110) that "a distribution in *liquidation of earnings* . . . does not constitute a dividend in the proper sense of the term" (italics ours), citing *Hellmich* v. *Hellman*. Since the result reached depended only on § 27(f), and since that provision is limited by its own terms to the computation of the dividends paid credit, it would seem to follow fairly directly that such a distribution is not "a taxable dividend" within other sections of the statute. See also *Commissioner* v. *Kay Mfg. Corp.*, 122 F.(2d) 443, 444-445 (C.C.A. 2d), certiorari denied, 316 U.S. 680.

Other cases which support the same conclusion include *Commissioner* v. *Cordingley*, 78 F.(2d) 118 (C.C.A. 1st); *Kelly* v. *Commissioner*, 97 F.(2d) 915 (C.C.A. 2d); *Hammans* v. *Commissioner*, 121 F.(2d) 4 (C.C.A. 2d); *Amelia H. Cohen Trust* v. *Commissioner*, 121 F.(2d) 689 (C.C.A. 3d); and *Malone* v. *Commissioner*, 128 F.(2d) 967 (C.C.A. 5th). When it is to the Commissioner's advantage to contend that a transaction of this sort is a partial liquidation, he makes that argument, and has been sustained.

In considering the *effect* of the transaction, the definition in § 115(i) of the statute points strongly in the same direction. Section 115(i) reads as follows:

> "*Definition of Partial Liquidation.* — As used in this section the term "amounts distributed in partial liquidation" means a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock.

It seems clear that the recapitalization in the present case had much more the effect of a partial liquidation, within the definition given in § 115(i) than it did of an ordinary taxable dividend to which § 115(a) would be applicable. If this is true, then the situation, being a recapitalization, is governed by § 112(c)(1) and not by § 112(c)(2).

The Government undertakes an answer to this point (Br. 49-51) which seems patently unsound. The contention is made that this transaction did not have the effect of a partial liquidation because "it was a complete cancellation of *all* the stock." This argument is completely formal and disregards the substance of the transaction. Under it many partial liquidations would be complete liquidations.[13] The section obviously does not apply where stock is replaced, dollar for dollar, with stock. That is not a "complete cancellation or redemption" of the old stock. But the section does apply where new stock is issued in exchange for old, in connection with a reduction of the capitalization of the company. That is a "complete cancellation or redemption of a part of its

13. If the Government's argument is sound (which we do not believe), then the transaction here was a complete liquidation. That is just as satisfactory to us as a partial liquidation; it does not have the *effect* of a taxable dividend. Of course it was not a complete liquidation; but it had the effect of a partial liquidation because a substantial part of the company's capital was eliminated.

stock," when it is borne in mind that "stock" in this connotation must mean the capital of the company, rather than the specific pieces of paper from time to time representing that capital.

If the Tax Court is to be regarded as the guardian of this part of the law, the course of its decisions would seem to be inconsistent with the result reached by the single judge in the present case. In *Holmby Corp.*, 28 B.T.A. 1092, the Board was concerned with a distribution made by a corporation which had earnings and profits, and which the taxpayer contended was an ordinary dividend (not taxable to a corporation). The Board held, however, that the distribution was "in partial liquidation", saying (p. 1102):

> A distribution may come within the broad definition of a "dividend" as defined in section 201(a) [§ 115(a)] *supra*, and yet at the same time be the very transaction specifically provided for in section 201(c) [§ 115(c), relating to partial liquidation] of the statute. *Langstaff* v. *Lucas*, 9 Fed.(2d) 691; affd., 13 Fed.(2d) 1022; *Hellmich* v. *Hellman*, 276 U. S. 233.

This was a decision of the full Board, without dissent. It was affirmed on appeal *Holmby Corp.* v. *Commissioner*, 83 F.(2d) 548 (C.C.A. 9th). The Appellate Court said (p. 549): "The fact that the distributions were called 'dividends' and were made, in part, from earnings and profits, and that some of them were made before liquidation or dissolution proceedings were commenced, is not controlling."

In *Tecla M. Straub*, 29 B.T.A. 216, 220, the Board declared:

> The evidence, in our opinion, establishes that the distribution of 1928 was made in partial liquidation of the corporation's capital stock. This is true notwithstanding the fact that the method was that of reducing the face value of each outstanding share

and not that of reducing the number of outstanding shares.

This decision was affirmed on appeal, and the above language was quoted with approval by the court. *Commissioner* v. *Straub*, 76 F.(2d) 388 (C.C.A. 3d).

The Board also found that there was a partial liquidation in *Benjamin R. Britt*, 40 B.T.A. 790. Much of its language is so closely applicable to the present case that it seems advisable to set it out here. It said (pp. 796-797):

> To be a partial liquidation it is not necessary that the corporation be planning a cessation of business or be in the process of final liquidation or that all of the preferred stock be retired at once. *Commissioner* v. *Quackenbos*, 78 Fed.(2d) 156; *Commissioner* v. *Cordingley*, 78 Fed.(2d) 118. In *Salt Lake Hardware Co.*, 27 B.T.A. 482, holding that amounts paid to redeem outstanding preferred stock constituted amounts distributed in partial liquidation, the Board said: "As set forth in the statute, section 201, *supra*, [the counterpart of section 115(i) in the 1934 Act] a partial liquidation takes place whenever a corporation distributes money or assets in complete cancellation or redemption of a part of its capital stock. No particular portion is mentioned, nor is the word 'part' in any way limited. Whether the amount so redeemed be all of a series or class, or only a part thereof, apparently makes no difference under the definition adopted by Congress." See also *Dill Manufacturing Co.*, 39 B.T.A. 1023.

Petitioner further contends that United Carbon Co. redeemed this stock out of profits, rather than capital, and that section 115 of the 1934 Act deals only with distributions which effect a change in the capital structure of the corporation. Implicit in this is the view that a distribution of profits can not be a partial

liquidation. The decision of the Supreme Court in *Helvering* v. *Chester N. Weaver Co.*, 305 U.S. 293, concludes the petitioner in that position. This cancellation of this stock did reduce its capital. When United Carbon Co. reacquired its stock, it canceled it, and could not reissue the shares acquired.

The decision in this case was affirmed on appeal, but on other grounds, without reference to the partial liquidation point. *Britt* v. *Commissioner*, 114 F.(2d) 10 (C.C.A. 4th).

Finally, reference should be made to the recent decision of the Tax Court in *Hamilton Allport*, 4 T.C. 401. The decision there, by Judge Sternhagen, contains the following clear statement (p. 403):

> This requirement had nothing to do with any plan which the corporation might have for an expansion or nonliquidation of its business. The statute applies, not to a distribution in liquidation of the corporation or its *business*, but to a distribution in cancellation or redemption of a part of its *stock*. (Italics in original.)

All of these decisions, we submit, are inconsistent with the Government's position in the present case.

None of the many cases cited by the Government on the construction of § 112(c)(2) involved a situation where the capital of the corporation was reduced as a part of the transaction. That is the essential element in this case, the factor which (a) distinguishes it from cases on which the Government relies, and (b) shows that the transaction did not have the *effect* of the distribution of a taxable dividend, but was more nearly akin to a distribution in partial liquidation.

The failure to recognize the fact that the cash paid here was paid in connection with the reduction of the corporation's capital runs through the Commissioner's whole

brief. When that fact is taken into account the Commissioner's argument and authorities become inapplicable. The "effect" of a cash payment in connection with a reorganization depends upon the nature and circumstances of the particular reorganization. Where a company sells out its tangible assets to another company in connection with a reorganization, and distributes its cash to its shareholders, the cash distribution may well have the effect of the distribution of a taxable dividend, as many of the Commissioner's cases show. But that is not what was done here. Here there was no selling out with an accompanying distribution of surplus. Instead there was a reduction of the corporation's capital. A payment made in connection with such a transaction "has the effect of" a partial liquidation rather than the distribution of an ordinary dividend, and thus is not within the language or the purpose of § 112(c)(2).

2. This leads to the *second* reason why the effect of the transaction was that of a liquidating dividend rather than that of an ordinary or taxable dividend. This is because the corporation could not legally declare an ordinary dividend at the time the transaction was carried out. It makes no difference that *if* the corporation could have declared a dividend it would have been taxable under § 115(a) since it had earnings and profits of the current year. The important fact is that the corporation could not declare a dividend under state law because its books showed a deficit in surplus. For this reason the corporation had in fact paid no dividends for more than five years before the transaction in question (R. 11-12). It is true that the Federal Revenue Act establishes a Federal test of when a dividend actually made by a corporation is taxable. But the Federal law does not establish a test which controls the question whether a corporation can declare a dividend. That is peculiarly a matter within the control of state law, to which the Federal law could hardly be applied, and as to which Congress has not

sought to make any provision. Since, in the present case, the corporation *could* not declare a taxable dividend, it is difficult to see how the transaction carried out could have the effect of what it could not do.

In the setting of the case, it is perfectly clear that the court below did not decide that the transaction *was* a partial liquidation. The question before the court was the *effect* of the distribution, and what it said in its opinion was obviously directed to that question.

The Government, however, misses the point, and includes in its brief (Br. 54-56) an argument that if the transaction *was* a partial liquidation, the amount received would be taxable in full. That is doubtless true. But no one has ever argued or suggested that the transaction *was* a liquidation. On the contrary, it has from the beginning been agreed by the parties that the transaction which was carried out was a recapitalization of the company, and that therefore the exchange which was made was in connection with a reorganization, and its tax consequences are governed by § 112(c) of the statute. All that we argue, and all that the court below put into its opinion, is designed to meet the contention of the Commissioner that the transaction had the *effect* of a taxable dividend. Our argument, therefore, is directed to the question of effect, and not to what the transaction was. There is no dispute on the latter question. But on the plane of effect, we argue, for the reasons given, that the effect of the transaction, if it had any other effect than that of the straightforward recapitalization it purported to be, was rather that of a distribution in partial liquidation than that of an ordinary taxable dividend. And if its effect is found to be that of a recapitalization, or of a distribution in partial liquidation, or anything else than an ordinary taxable dividend, then § 112(c)(2) has no application to the present case.

E. The Committee Reports and Regulations Show the Inapplicability of § 112(c)(2)

Resort to the legislative history of § 112(c)(2) supports the same conclusion. It shows that § 112(c)(2) was designed to apply to transactions which amounted in substance to devices for the distribution of an ordinary dividend with no other legitimate purpose or effect. The provision now found in § 112(c)(2) first made its appearance as § 203(d)(2) of the Revenue Act of 1924, and it has remained without change since that time. The purpose of that provision was explained in substantially identical language in the Committee Reports. (House Report No. 179, 68th Congress, 1st Session, pp. 14-15, reprinted in 1939-1 Cum. Bull. Part 2, pp. 241, 252; Senate Report No. 398, 68th Congress, 1st Session, pp. 15-16, reprinted in 1939-1 Cum. Bull. Part 2, pp. 266, 277.) This passage reads as follows:

> (2) There is no provision of the existing law which corresponds to paragraph (2) of subdivision (d). This paragraph provides that any amount distributed by a corporation in connection with a reorganization which has the effect of a taxable dividend shall be taxed as a dividend.
>
> The necessity for this provision may best be shown by an example: Corporation A has capital stock of $100,000, and earnings and profits accumulated since March 1, 1913, of $50,000. If it distributes the $50,000 as a dividend to its stockholders, the amount distributed will be taxed at the full surtax rates.
>
> On the other hand, corporation A may organize corporation B, to which it transfers all its assets, the consideration for the transfer being the issuance by B of all of its stock and $50,000 in cash to the stockholders of corporation A in exchange for their stock in corporation A. Under the existing law, the $50,000

distributed with the stock of corporation B would be taxed, not as a dividend, but as a capital gain, subject only to the 12½ per cent rate. The effect of such a distribution is obviously the same as if the corporation had declared out as a dividend its $50,000 earnings and profits. If dividends are to be subject to the full surtax rates, then an amount so distributed should also be subject to the surtax rates and not to the 12½ per cent rate on capital gain.

This statement shows that the situation to which Congress directed § 112(c)(2) was essentially different from that presented in the present case. The example given is that of a corporation with surplus available for distribution as a dividend, and with no restriction on its power to declare those earnings as a taxable dividend. Instead of making such a declaration, however, it goes through the form of a reorganization, similar to that struck down in *Gregory* v. *Helvering*, 293 U.S. 465, the sole purpose and effect of which is to distribute the earnings and profits to the shareholders without altering their capital investment in the company. In the present case, however, the company was legally disabled from declaring a taxable dividend. The transaction which it carried out was no sham. It was obviously designed for a bona fide business purpose, so that the corporation might reestablish its credit and put itself into condition so that it might declare dividends. No contention has even been made to the contrary. Moreover, the transaction here involved an actual reduction in the capitalization of the company. The stake of each preferred stockholder in the venture was reduced while in the situation mentioned in the Committee Report the capital investment of the shareholder remained unchanged.

Similarly, the only provision in the Regulations which bears on § 112(c)(2) shows that it has no application to the present case. This is found in Art. 112(g)-4 of

Regulations 94, issued under the Revenue Act of 1936.[14] It merely repeats the language of the statute, and then sets out the same example as that given in the Committee Report, thus showing the Commissioner's understanding that § 112(c)(2) applies only to essentially sham transactions, where the stockholders' capital investment in the enterprise remains unchanged. This Regulation continues in effect to the present time without change. See § 29.112(c)-4 of Regulations 111.

Thus the legislative history and the Regulations show that § 112(c)(2) was designed to reach a different sort of transaction than that involved here, and particularly that it was not intended to apply to transactions which have the effect of liquidating dividends rather than of ordinary taxable dividends.

F. The Government's Position Leads to Incongruities

The fact that the taxpayer here received cash in connection with the transaction does not mean that he received

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14. The full text of the applicable passage reads as follows:

> If the distribution of such other property or money by or on behalf of a corporation in the course of a reorganization has the effect of the distribution of a taxable dividend, then, as provided in section 112(c)(2), there shall be taxed to such distributee (1) as a dividend, such an amount of the gain recognized on the exchange as is not in excess of the distributee's ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913, and (2) the remainder of the gain so recognized shall be taxed as a gain from the exchange of property.
>
> *Example:* The X Corporation has a capital of $100,000 and earnings and profits of $50,000 accumulated since February 28, 1913. The X Corporation in 1936 transfers all of its assets to the Y Corporation in exchange for the issuance of all of the stock of the Y Corporation and the payment of $50,000 in cash to the stockholders of the X Corporation. A, who owns one share of stock in the X Corporation, for which he in 1928 paid $100, receives a share of stock in the Y Corporation worth $100 and the sum of $50 in cash in addition. A is liable to both the normal tax and the surtax on $50.

taxable income. It is the normal thing to receive cash in connection with a capital transaction. If a person owns shares and sells them, he receives cash, and has a capital gain or loss. Section 112(b)(3) of the statute provides for the non-recognition of *gain or loss* on an *exchange* of stock in connection with a reorganization. The basic transaction is an *exchange*. It is a typical capital transaction. It is just what happened here. The present taxpayer gave up securities, and received in exchange therefor, other securities and cash. Thus, if there were no special statutes affecting the situation, there would clearly have been a capital gain on an *exchange*. See *Cullinan* v. *Walker*, 262 U.S. 134; *Marr* v. *United States*, 268 U.S. 536. But Congress has intervened in this situation and provided that no gain or loss shall be recognized on such an exchange in connection with a reorganization (§ 112(b)(3)), with the further qualification that if cash is received on the exchange, then the gain shall be recognized, but only to the amount of the cash received. Section 112(c)(1). But the gain so recognized still remains *capital gain* realized on an *exchange*. This is the basic normal situation. Section 112(c)(2) then provides that if the cash received had "the effect of the distribution of a taxable dividend" it shall be taxed as a dividend. But it by no means follows, as the Government has argued, that all cash received in connection with a reorganization has the effect of a dividend. Throughout its brief, the Government constantly overlooks the essentially capital nature of the transaction which was carried out here. By common consent, it was a *recapitalization*.

In the present case, the taxpayer had a gain on the exchange. Let us consider, however, the case of a shareholder who had a *loss* on such an exchange as that involved here, that is, one whose cost basis was higher than the amount of securities and cash which he received in the exchange. Such a taxpayer would receive cash to the same extent as the taxpayer here. Yet it is clear that the cash received would not be taxable to him as a dividend.

Thus, the Government's argument here leads to the incongruous result that some stockholders would receive a dividend and some would not, on the very same transaction, depending not on what was done, but on what their cost basis happened to be.

The real difficulty with this position stands out when it is considered from the point of view of the corporation. If the transaction is a dividend here, it must involve a distribution of earnings and profits. Yet there would be the same distribution of earnings and profits in the case of a stockholder who had a loss; but in such a case there clearly would be no dividend. Thus the Government's argument involves the conclusion that there can be a distribution of earnings and profits which is not a dividend. It seems doubtful whether the Government would accept that position directly, despite the statement in its Brief (p. 48).

The Government suggests this difficulty in the last paragraph of its brief (Br. 60), but does not directly face it. It points up, however, a basic incongruity in the Government's position, which can be avoided by recognizing that the transaction here involved was a capital transaction, having the effect of a partial liquidation, and not involving either the paying out of earnings and profits by the corporation or their receipt by the taxpayer. *Cf. Bass* v. *Commissioner*, 129 F.(2d) 300 (C.C.A. 1st).

CONCLUSION

This Court does not have jurisdiction of the petition. If it does, the judgment below is correct and should be affirmed.

Respectfully submitted,

ERWIN N. GRISWOLD,
HOLT S. McKINNEY,
Counsel for Respondent.

March, 1945.

APPENDIX

Certificate of Clerk of Circuit Court of Appeals

UNITED STATES CIRCUIT COURT OF APPEALS

SECOND CIRCUIT

ESTATE OF EDWARD T. BEDFORD,
Title Guarantee & Trust Company, Executor,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

I, ALEXANDER M. BELL, Clerk of the United States Circuit Court of Appeals, for the Second Circuit, do hereby certify that the docket entries in the above entitled case in this Court are as follows:

August	19, 1943	Filed Record
August	31, 1943	Filed order extending time
October	7, 1943	Filed 24 copies, record
October	7, 1943	Filed brief, petitioner
October	22, 1943	Filed appearance, Comnr by J. P. Wenschek, et al.
December	15, 1943	Filed appearance, Comnr by S. O. Clark, Jr., et al.
December	15, 1943	Filed brief, respondent.
January	3, 1944	Filed brief, petitioner, reply
August	8, 1944	Order reversed, A. N. Hand, *C. J.*
August	29, 1944	Filed order for mandate
August	29, 1944	Issued mandate
October	13, 1944	Certified record to Sol Gen'l
December	2, 1944	Filed notice.

Dated, New York, December 8, 1944.

ALEXANDER M. BELL,
Clerk, United States Circuit Court
of Appeals.

[Seal]

SUPREME COURT OF THE UNITED STATES.

No. 710.—October Term, 1944.

Commissioner of Internal Revenue, Petitioner, *vs.* Estate of Edward T. Bedford, Title Guarantee and Trust Company, Executor.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[May 21, 1945.]

Mr. Justice Frankfurter delivered the opinion of the Court.

At the threshold, the jurisdiction of the Court is challenged on the ground that the petition for the writ of certiorari was not filed within three months after "entry" of the "judgment" below as required by the Judiciary Act of February 13, 1925.[1]

The steps by which the case came here are these. On August 8, 1944, the Circuit Court of Appeals for the Second Circuit filed a document entitled "Opinion"; on the same day the Clerk made a docket entry reading, "Order reversed, A. N. Hand, *C.J.*"; on August 29, 1944, a document entitled "Order for Mandate" was filed, and the mandate issued that day; on November 29, 1944, the petition for writ of certiorari was filed. The petition was filed too late if the "Opinion", as respondent contends, constitutes the "judgment". It was filed in time, if the "Order for Mandate" may properly be deemed the "judgment". The issue was ably pressed before us, and, since it concerns our power to review cases coming from what is perhaps the busiest circuit, it calls for more than summary treatment.

Even long continued practice cannot alter the limits within which Congress has bound the appellate judisdiction of this Court. See *Dept. of Banking* v. *Pink*, 317 U. S. 264. But such prac-

[1] "Sec. 8(a) That no writ of error, appeal, or writ of certiorari, intended to bring any judgment or decree before the Supreme Court for review shall be allowed or entertained unless application therefor be duly made within three months after the entry of such judgment or decree, excepting that writs of certiorari to the Supreme Court of the Philippine Islands may be granted where application therefor is made within six months: *Provided*, That for good cause shown either of such periods for a writ of certiorari may be extended not exceeding sixty days by a justice of the Supreme Court." 43 Stat. 936, 940, 28 U. S. C. § 350.

tice may be decisive in interpreting procedural ways which, as a matter of dialectic or abstract analysis, may appear dubious. We are naturally impressed by the common understanding that in the Circuit Court of Appeals for the Second Circuit the so-called "Order for Mandate" is deemed the judgment. Robertson and Kirkham, Jurisdiction of the Supreme Court of the United States (1936) § 384. We have taken and decided as a matter of course a considerable number of cases in which certiorari was sought within three months after entry of the "Order for Mandate" but not within three months after the "Opinion".[2] This practical understanding of the controlling significance, for appellate purposes, of the "Order for Mandate" is supported and certainly not contradicted by all that is conveyed by the "Opinion" and "Order for Mandate" and the Rules of the lower court.

It does not detract from the "Opinion" as an opinion that in its heading it gives as dates "Argued January 6, 1944
Decided August 8, 1944", and that it concludes with "The order of the Tax Court is reversed." The same or similar phrases are commonly employed in opinions of this Court without changing their character as opinions. Nor do like phrases in the opinions of the other circuit courts of appeals turn them into judgments, since in all other circuits judgment orders are separately filed. In spite of its title, the "Order for Mandate" on its face fulfills the function of such a judgment order. It recites that

"it is now hereby ordered, adjudged, and decreed that the order of said The Tax Court of the United States be and it hereby is reversed.

It is further ordered that a Mandate issue to the said The Tax Court of the United States in accordance with this decree.

Alexander M. Bell,
Clerk.

By A. Daniel Fusaro,
Deputy Clerk."

This language plainly imports that this is the judgment and that it is then being rendered. Nor does the fact that the order was

[2] During the 1941, 1942 and 1943 Terms, this Court entertained reviews and affirmed judgments of the Circuit Court of Appeals for the Second Circuit in not less than ten such cases: Commercial Corp. *v.* N. Y. Barge Corp., 314 U. S. 104; New York *v.* United States, 315 U. S. 510; Mother Lode Co. *v.* Comm'r, 317 U. S. 222; Smith *v.* Shaughnessy, 318 U. S. 176; Helvering *v.* Griffiths, 318 U. S. 371; Emil *v.* Hanley, 318 U. S. 515; Fisher Co. *v.* Witmark & Sons, 318 U. S. 643; Equitable Society *v.* Comm'r, 321 U. S. 560; Medo Corp. *v.* Labor Board, 321 U. S. 678; United States *ex rel.* Irensilber *v.* Bausch & Lomb Optical Co., 320 U. S. 711 (equally divided court).

prepared by the clerk and bears his signature detract from its quality as a judgment. A judgment "is the act of the court", *Ex parte Morgan*, 114 U. S. 174, 175, even though a clerk does all of the ministerial acts, as here, in conformity with his court's standing instructions.

The Rules of the court below governing opinions, rehearings, issuance of mandate and stay of mandate are invoked to show that the "Opinion" is the appealable "judgment". These Rules, like other rules, are not phrased with such fastidious precision as to make of all the parts a perfect harmony. But while substantial debating points may be taken,[3] nothing in these Rules contradicts the natural meaning yielded by the terms of the "Opinion" and the "Order of Mandate", as reflected in the practice of the Second Circuit and in our own, which treats not the "Opinion" but the "Order for Mandate" as the order of judgment. The Rules would have to be far less artistic than they are to warrant us in holding that the Circuit Court of Appeals has consistently misinterpreted some of its own Rules. Whether the announcement of an opinion and its entry in the docket amounts to a judgment for purposes of appeal or whether that must await some later formal act, ought not to be decided on nice-spun argumentation in disregard of the judicial habits of the court whose judgment is called into question, of the bar practising before it, of the clerk who embodies its procedural traditions, as well as in conflict with the assumption of the reviewing court.

But now that the existing practice has revealed abstract disharmonies, if not difficulties, the Circuit Court of Appeals will doubtless establish a more tidy system for meeting the technical requirements for review here. The normal time for entering a

[3] Respondent argues that the Rules of the court below, with respect to the opinions of the court, rehearings, issuance of mandate, and stay of mandate, show that the "opinion" is meant to constitute the court's judgment. But these Rules compute time, with respect to filing of petitions for rehearing and for issuance of mandate, not from entry of a "judgment" but from the "filing of the opinion of this court". Some difficulty is raised because Rule 27 refuses a rehearing "unless a judge who concurred in the judgment desires it." Also respondent finds it paradoxical to "stay" the court's mandate under Rule 30 when the mandate is customarily issued on the same day the "Order for Mandate" is filed. And respondent argues that the court could not have meant to confer upon its clerk discretion to hold up, for varying lengths of time, the rendering of a judgment until fees have been paid by the prevailing party. In this case the "Order for Mandate" and issuance of the mandate were delayed for twenty-one days, and were not entered within fifteen days from the filing of the opinion which Rule 30 requires; the time has been variously extended in other cases.

and the court's instructions

judgment, as the starting point for determining whether review will be sought or whether there has been acquiesence in a judgment, should be fixed. The uncertainties inherent in litigation should not be needlessly prolonged. The entry of the "Order for Mandate", which in the Second Circuit begins the running of the period for appeal, is apparently variable and vagrant. In these days of rapid communication, the statutory allowance of three months is more than ample for an unsuccessful litigant to determine whether to seek further review. So long a period ought not to be extended by delay in entering a judgment nor should the burden of securing such entry be put upon the successful litigant. There are bound to be diversities in the modes of rendering and recording judgments of the forty-eight systems of State courts. Uniformity in the entry of judgment among the eleven circuits forming the single federal judicature ought to be capable of achievement without loss to the geographic flexibility of the system.

This brings us to the merits, which involve the validity of an income tax deficiency assessment for 1937. The case is this. The estate of Edward T. Bedford, who died May 21, 1931, included 3,000 shares of cumulative preferred stock (par value $100) of Abercrombie & Fitch Company. Pursuant to a plan of recapitalization respondent, as executor of the estate, in 1937 exchanged those shares for 3,500 shares of cumulative preferred stock (par value $75), 1,500 shares of common stock (par value $1), and $45,240 in cash (on the basis of $15.08 for each of the old preferred shares). The recapitalization had been proposed because the company, after charging against its surplus account stock dividends totaling $844,100, distributed in 1920, 1928, and 1930, had incurred a book deficit in that account of $399,771.87. Because of this deficit, the company, under applicable State law, was unable to pay dividends although for the fiscal year ending January 31, 1937 it had net earnings of $309,073.70.

By comparing the fair market value of the old preferred shares at the date of Bedford's death with the market value of the new stock and cash received the gain to his estate was $139,740. Admittedly the recapitalization was a reorganization, § 112 (g) (1) (D) of the Revenue Act of 1936, 49 Stat. 1648, 1681, 26 U. S. C. § 112(g) (1) (E), so that only the cash received, but none of the stock, is taxable. Sections 112(b) (3), 112(c) (1), 49 Stat. 1648.

1679, 1680, 26 U. S. C. §§ 112(b)(3), 112 (c)(1). The sole issue is whether the cash, $45,240, is taxable as a dividend, or merely as a capital gain to the extent of 40%. The Tax Court sustained the determination of the Commissioner that the cash was taxable as a dividend, 1 T. C. 478, but was reversed by the Circuit Court of Appeals. 144 F. 2d 272. On a showing of importance to the administration of the Revenue Acts, we granted certiorari. — U. S. —.

The precise question is whether the distribution of cash in this recapitalization "has the effect of the distribution of a taxable dividend" under § 112(c)(2) of the Revenue Act of 1936 and as such is fully taxable, or is taxable only at the rate of 40% as a capital gain under § 112(c)(1) of that Act. The relevant provisions read: "(c) *Gain from Exchanges not Solely in Kind.*— (1) If an exchange would be within the provisions of subsection (b), (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property. (2) If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his rateable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property."

The history of this legislation is not illuminating. Section 112(c)(2) originated in § 203(d)(2) of the Revenue Act of 1924, 43 Stat. 253, 257. But the reports of the Congressional Committees merely use the language of the section to explain it. H. Rep. No. 179, 68th Cong., 1st Sess., pp. 14-15; S. Rep. No. 398, 68th Cong., 1st Sess., pp. 15-16. Nor does the applicable Treasury Regulation add anything; it repeats substantially the Committee Reports. Treas. Reg. 94, Art. 112 (g)-4. We are thrown back upon

the legislative language for ascertaining the meaning which will best accord with the aims of the language, the practical administration of the law and relevant judicial construction.

Although Abercrombie & Fitch showed a book deficit in the surplus account because the earlier stock dividends had been charged against it, the parties agree that for corporate tax purposes at least earnings and profits exceeding the distributed cash had been earned at the time of the recapitalization. That cash therefore came out of earnings and profits and such a distribution would normally be considered a taxable dividend, see § 115(a),[4] and has so been treated by the courts in seemingly similar situations. It has been ruled in a series of cases that where the stock of one corporation was exchanged for the stock of another and cash and then distributed, such distributions out of earnings and profits had the effect of a distribution of a taxable dividend under § 112(c)(2). *Comm'r* v. *Owens*, 69 F. 2d 597; *Comm'r* v. *Forhan Realty Corp.*, 75 F. 2d 268; *Rose* v. *Little Inv. Co.*, 86 F. 2d 50; *Love* v. *Comm'r*, 113 F. 2d 236; *Campbell* v. *United States*, 144 F. 2d 177. The Tax Court has reached the same result, that is, has treated the distribution as a taxable dividend, in the case of the recapitalization of a single corporation. *McCord* v. *Comm'r*, 31 B. T. A. 342, 344; *J. Weingarten, Inc.* v. *Comm'r*, 44 B. T. A. 798, 808-809; *Knapp Monarch Co.* v. *Comm'r*, 1 T. C. 59, 69-70, affirmed on other grounds, 139 F. 2d 863. We cannot distinguish the two situations and find no implication in the statute restricting § 112(c)(2) to taxation as a dividend only in the case of an exchange of stock and assets of two corporations.

Respondent, however, claims that this distribution more nearly has the effect of a "partial liquidation" as defined in § 115(i).[5]

[4] "(a). *Definition of Dividend.*—The term 'dividend' when used in this title (except in section 203(a)(3) and section 207(c)(1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made."

[5] "(i). *Definition of Partial Liquidation.*—As used in this section the term 'amounts distributed in partial liquidation' means a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock."

But the classifications of § 115, which governs "Distributions of Corporations" apart from reorganizations, were adopted for another purpose. They do not apply to a situation arising within § 112. The definition of a "partial liquidation" in § 115(i) is specifically limited to use in § 115. To attempt to carry it over to § 112 would distort its purpose. That limitation is not true of § 115(a) which defines "dividend" for the purpose of the whole title. Accordingly, this definition is infused into § 112(c)(2). Under § 115(a) a distribution out of accumulated earnings and profits is a "dividend", thus confirming the conclusion that a distribution of earnings and profits has the "effect of the distribution of a taxable dividend" under § 112(c)(2).

Recapitalization does not alter the "effect". Although the capital of a company is reduced, the cash received is a distribution of earnings and profits and as such falls within the federal tax. That the company's treatment of its stock dividends may bring consequences under State law requiring a capital reduction does not alter the character of the transactions which bring them within the federal income tax. Recapitalization is one of the forms of reorganization under § 112(g)(1)(D). It cannot therefore be urged as a reason for taking the transaction out of the requirements of § 112 and forcing it into the mold of § 115. The reduction of capital brings § 112 into operation and does not give immunity from the requirements of § 112(c)(2).

Treating the matter as a problem of statutory construction for our independent judgment, we hold that a distribution, pursuant to a reorganization, of earnings and profits "has the effect of a distribution of a taxable dividend" within § 112(c)(2). As is true of other teasing questions of construction raised by technical provisions of Revenue Acts the matter is not wholly free from doubt. But these doubts would have to be stronger than they are to displace the informed views of the Tax Court. And if the case can be reduced to its own particular circumstances rather than turn on a generalizing principle we should feel bound to apply *Dobson* v. *Commissioner*, 320 U. S. 489, and sustain the Tax Court.

Reversed.